ORIGINAL

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
International Settlement Rates	)	File No. IB 96-261

AT&T REPLY TO OPPOSITIONS TO
PETITION FOR PARTIAL RECONSIDERATION

AT&T Corp. ("AT&T"), in accordance with Section 1.429 (g) of the Commission's Rules, hereby submits its Reply Comments to the Oppositions filed by GTE Service Corp. ("GTE"), the Philippines Parties, Sprint Communications Company L.P. ("Sprint") and Telefonica International De Espana ("Telefonica") to AT&T's Petition For Partial Reconsideration in the above-referenced proceeding.

As AT&T demonstrated in its Petition, only "best practice" rather than benchmark rates can reliably prevent the competitive harm found by the Commission to be caused by above-cost settlement rates where services are provided on affiliate routes. There is no showing that any alternative approach will adequately address the potential dangers identified by the Commission.

If the Commission declines to adopt a fully preventive remedy in the form of best practice settlement rates, it should ensure that its *ex post* enforcement mechanism will adequately address predatory pricing. Indeed, there is no substantive opposition to the second basis for partial reconsideration set forth by AT&T's petition: that the average variable cost bright line pricing test for outbound facilities-based distortion should reflect

the predatory pricing standard used elsewhere by the Commission, which takes account of *all* variable costs attributable to the relevant service.[1] The Commission should revise this critical safeguard accordingly to provide more effective protection against below-cost pricing.

I. A FULLY PREVENTIVE APPROACH REQUIRES THE USE OF 'BEST PRACTICE' RATES.

While several parties object to AT&T's request that the Commission condition Section 214 authorizations on adherence to the "best practice" rate rather than on adoption of benchmark settlement rates, none has sought reconsideration of the Commission's key *Benchmark Order* findings: (1) that carriers with above-cost settlement rates providing switched services on affiliate routes may engage in price squeezes (¶¶ 208, 219) and/or raise competitors' costs through one-way by-pass (¶ 242): and (2) that requiring settlement rates to be lowered to benchmark levels is a necessary preventive measure to reduce such competitive harm (¶¶ 211, 243, 248).[2] Nor is there any showing

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1 The Philippines Parties (pp. 4-5) question AT&T's concern with price squeezes and oppose both of AT&T's proposed changes on these grounds, but express no specific disagreement with AT&T's proposed revisions to the bright line pricing test. No other party addresses this second issue on which AT&T has sought reconsideration.

2 Sprint offers no support for its claim (pp. 7-8) that a price squeeze can only occur where settlement rates are "substantially" above cost. Such behavior is also possible at lower margins, as the Commission has found with respect to domestic access charges. Further, incentives to increase the volume of U.S.-outbound minutes on which settlements are paid may increase, rather than diminish, as the per minute settlement rate is decreased. Many of Telefonica's claims concerning the supposed lack of rationality of price squeeze behavior have been addressed in the *Foreign Participation* proceeding. *See Rules and Policies on Foreign Participation in the U.S. Telecommunications Market*, File No. IB 97-142, Reply Comments of AT&T, dated August 12, 1997, Attachment 2 (Memorandum from William Lehr, dated Aug. 4, 1997). Others do not withstand scrutiny -- such as Telefonica's unfounded

(footnote continued on following page)

in opposition to AT&T's Petition that *ex post* enforcement action -- with its attendant difficulties in detection, delays and additional costs -- will adequately address the incentives for misconduct that will continue notwithstanding the adoption of benchmark rates.[3]

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contention (p. 6) that "virtually all" customers select carriers on the basis of prices for domestic long distance and "all international routes." In fact, most residential international callers focus on the handful (at most) of countries in which they have family or friends. Similarly, any prior absence of price squeeze behavior (p. 9) is not dispositive, as the relatively small number of foreign carriers now present in the U.S., particularly from closed markets, may believe themselves to be more easily scrutinized than the larger numbers that will enter after 1998. Also, the few foreign-owned carriers present in the U.S., both resellers and facilities-based carriers, were subject to dominant carrier regulation until 1992 requiring longer notice periods for tariffs and cost support for tariff filings. Telefonica remained subject to such requirements until late 1995. There is also no basis to Telefonica's arguments that a "best practice" settlement rate condition would violate GATS requirements. *See, e.g., Benchmark Order*, ¶ 264; *Rules and Policies on Foreign Participation in the U.S. Telecommunications Market*, File No. IB 97-142, Reply Comments of the Office of the U.S. Trade Representative, filed Oct. 17, 1997; *id.*, AT&T Reply Comments, filed Aug. 12, 1997, at 30,n.50.

GTE improperly seeks to obtain reconsideration of a new issue raised for the first time in its Opposition to AT&T's Petition -- that existing holders of Section 214 authority should be provided transition periods to benchmark rates on affiliated routes. GTE's request does not comply with the Section 1.429 requirement that reconsideration of Commission action should be sought through a petition for reconsideration, rather than an opposition, and should accordingly be stricken as procedurally improper and untimely. In any event, GTE fails to justify the different treatment it seeks for existing Section 214 holders. As the Commission has emphasized, "[t]he same concerns about anticompetitive behavior we seek to address through our conditions apply equally to carriers with existing authorizations." *Benchmark Order*, ¶ 228. Without clear evidence that these concerns are limited to new Section 214 holders, the Commission should apply the rule as required by the *Benchmark Order*.

[3] *See* AT&T Petition at 6.

As demonstrated by AT&T's Petition (pp. 3-7), a fully preventive approach, requiring the removal of the U.S. subsidy payments that provide these incentives, is both consistent with WTO rules and would ensure that consumers derive maximum benefits from the provision of service on affiliated routes.

II. THE COMMISSION SHOULD REVISE THE BRIGHT LINE PRICING TEST.

AT&T has also sought partial reconsideration of the *Benchmark Order* on a second issue -- and on which no party expresses any specific disagreement: the need to revise the bright line pricing test for market distortion to conform to Commission precedent on predatory pricing matters. Rather than being limited to the net settlement rate and any originating access charges, as described by the *Benchmark Order* (¶ 224), the market distortion pricing test should include *all* variable costs attributable to the relevant service, including billing and collection, marketing, customer service, and relevant cost increments in plant investment and network maintenance.[4] The use of this definition of average variable cost, which is equivalent to total service long-run incremental cost, or average incremental cost, is required to prevent prices from being reduced far below both the levels the Commission has previously determined to be predatory and those required by U.S. antitrust precedent.[5]

As demonstrated by AT&T's Petition, and no party disagrees, absent the proposed revision, the bright line pricing test would not provide effective protection

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4 *See* AT&T Petition at 9-10; *PanAmSat Corp. v. Comsat Corp.*, File No. E-96-21, memorandum, Opinion and Order, (released May 20, 1997), ¶ 17. 1997 LEXIS 2657, *11.

5 *See* AT&T Petition at 9-11.

against predatory pricing conduct that would inflict severe losses on other carriers and "ultimately reduce the level of competition on particular international routes." *Benchmark Order*, ¶ 220. The Commission should revise this safeguard accordingly.

CONCLUSION

For the reasons explained in AT&T's Petition and in this Reply, AT&T respectfully requests the Commission to require adherence to the "best practice" settlement rate where service is provided on affiliate routes and to revise the average variable cost "bright line" test for outbound facilities-based distortion to include all variable or incremental costs attributable to the relevant service.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, Helen Elia, do hereby certify that on this 6th day of November, 1997 a copy of the foregoing "AT&T Reply to Oppositions to Petition for Partial Reconsideration" was mailed by U.S. first class mail, postage prepaid, upon the parties on the attached service list:

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